May 1, 2003

The Honorable Michael K. Powell
Chairman
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

The Honorable Michael J. Copps
Commissioner
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

The Honorable Kathleen Q. Abernathy
Commissioner
Federal Communications Commission
445 12th Street SW
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The Honorable Kevin J. Martin
Commissioner
Federal Communications Commission
445 12th Street SW
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The Honorable Jonathan S. Adelstein
Commissioner
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Re: *In the Matter of AT&T Corp. Petition for Rulemaking To Reform Regulation Of Incumbent Local Exchange Carrier Rates For Interstate Special Access Services*, RM Docket No. 10593.

Dear Mr. Chairman and Commissioners:

Four years ago, the Bell Operating Companies promised that they would lower their rates for the "special access" services that are essential building blocks for the entire spectrum of communications services, if only the Commission would relieve them of price cap limits on their rates for those services. The Bells assured the Commission (and their captive business and carrier customers) that this "pricing flexibility" was appropriate, because competitors would build facilities to customer locations that were then served only by the Bells, and that the threat of this future competition would hold the Bells to their promises of lower overall rates. And, although the Bells were always free to *lower* their special access rates, they claimed that relief from price caps was not merely appropriate, but absolutely necessary to allow them to "meet competition" from new entry that they claimed was already extensive and rapidly growing.

Four years later, it is painfully clear the Commission's decision to allow rate deregulation to precede actual price-constraining competition has been a failure of astounding proportions that the Commission must immediately remedy. The facilities-based competition that the Bells predicted and upon which the Commission relied simply has not materialized – "last mile" access to the vast majority of customer locations in the United States remains available *only* from the Bells or other incumbent providers. As the Commission recently reaffirmed in announcing its Triennial Review decision, the situation is not improving, because it is rarely economically

feasible for competitors to deploy alternative facilities, particularly the loops or, in special access parlance, "channel terminations" that are overwhelmingly supplied by the Bells.

As a result, the Bells have used pricing flexibility only to fill their own coffers at the expense of competition and customers, in direct violation of the core Communications Act requirement of just and reasonable rates. The rates for the Bells' special access prices have increased and their rates of return for special access services have soared, even as the unit costs of providing these services have sharply declined with technological advances and greatly increased demand.

Although the Bells' were granted "pricing flexibility" to "meet competition," their unregulated special access rates in supposedly "competitive" markets are uniformly now well in excess of their price-capped rates in markets where all acknowledge that the Bells face no meaningful competition. And even for the relative handful of point-to-point routes where there are facilities-based special access alternatives, the Bells feel no compulsion to lower rates to meet the competition. The Bells are earning special access returns that are triple, quadruple, *even quintuple*, the rate of return that the Commission found just and reasonable for dominant incumbent LEC services in 1990 at a time when inflation and capital costs were many times higher than today. And the Bells' rates continue to rise as their costs continue to fall.

Contrary to the Bells' rhetoric, this is not merely an interexchange carrier problem, although that alone would justify immediate Commission action given the well-documented declines of all IXCs except those for which bloated special access charges are merely a "left pocket, right pocket" transaction – the Bells. Rather, as the American Petroleum Institute, the eCommerce & Telecommunications Users Group, and the National Retail Federation have previously explained,[1] those suffering under special access "pricing flexibility" run the gamut from American businesses, large and small, that purchase special access directly and indirectly to virtually all of the nation's communications providers (including wireless and wireline, narrowband and broadband, ISPs and carriers, and local, long distance and international service providers), government agencies and, ultimately, American consumers nationwide; and the costs are staggering. The Bells' special access rates amount to an over *$5 billion annual tax*.

The undersigned members of the Special Access Reform Coalition (SPARC), which reflects the diversity of the Bells' special access victims, respectfully submits that the Commission has a clear obligation to make special access rate reform among its very highest priorities. Not only do the Bells' special access charges cause a severe misallocation of resources, they unquestionably stifle investment and innovation, including the very broadband investment and innovation that the Commission has identified as a top priority.

The Bells' special access abuses also pose a serious threat to existing competition in each of the "downstream" wireline and wireless markets that rely upon special access. Carriers of all types, narrowband and broadband, are dependent upon the Bells' special access services as critical inputs to the finished services that they provide at retail.[2] But as the Bells are granted

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[1]October 15, 2002, Letter from American Petroleum Institute, eCommerce & Telecommunications Users Group and the National Retail Federation to Chairman Powell, submitted in RM-10593.

[2] Nextel reply at 2-3.

authority to compete in these downstream markets, they increasingly have both the incentive and ability to use their special access market power to price squeeze their competitors and to provide them with inferior quality access.

It is well past time for Commission action in this area. The Commission should act now both to begin the process of adopting the comprehensive, permanent reforms that are necessary to protect customers from the Bells' market power and to provide the immediate interim relief necessary to mitigate public interest harms until permanent reform is completed.

**The Problem.** As demonstrated time and again, where it is able to do so, a Bell will charge monopoly rates, because monopoly rates are, by definition, profit-maximizing rates. There are only two possible constraints on such anticompetitive behavior: price-constraining competition or regulation. With respect to the Bells' special access services that have been rate deregulated (as most now have), it is now quite obvious that neither constraint exists. The Bells have special access monopolies to the vast majority of customer locations even in areas where they have been granted Phase II pricing flexibility (and hence are no longer subject to rate regulation). And, as the Bells themselves have recognized, market forces can constrain the Bells' special access pricing behavior only where customers "have economically realistic alternatives to RBOC special access facilities."[3]

The record in this proceeding contains overwhelming evidence that the hoped-for alternatives that were the underpinning for special access rate deregulation simply have not materialized. For example, AT&T demonstrated that it is able to use either its own or a competitive LEC's facilities in only about *five percent* of buildings.[4] Despite an aggressive program to purchase special access from competitive carriers, "non-ILEC vendors have accounted for only approximately 10% of Cable & Wireless' new installations for the year 2002, *down* from approximately 13% in 2001."[5] And "Sprint Long Distance . . . continues to rely upon the ILECs for approximately 93% of its total special access needs despite aggressive attempts to self-supply and switch to CLEC-provided facilities wherever feasible."[6] Wireless carriers have demonstrated that they, too, are dependent upon the Bells.[7] In short, except for the handful of customer locations that can justify an OCn level facility, competitive carriers usually have *no option* but the Bells for last mile access.

That is why no Bell has reduced *any* special access rate to meet competition on *any* point-to-point route, notwithstanding that competitive carriers are offering very substantial discounts off the corresponding Bell rates on the small minority of routes where it is economically feasible

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[3] Kahn-Taylor Dec. at 20 (attached to Verizon, Qwest, BellSouth and SBC comments).

[4] AT&T Petition, Thomas Dec. ¶ 3.

[5] Cable & Wireless at 13.

[6] Sprint at 3.

[7] *See, e.g.*, AT&T Wireless at 3 ("AWS has previously pointed out, for example, that more than ninety percent (90%) of its transport costs go to paying ILECs for special access services. Voicestream reported that ninety six percent (96%) of the circuits it uses to connect its mobile switching centers to cell site base stations are provided by the ILECs"). *See also* Nextel Reply at 1.

to bypass the Bells' facilities.[8] In fact, Verizon, BellSouth and Qwest have *raised* DS-level rates in *every* single one of their Phase II pricing flexibility MSAs (*i.e.*, those MSAs that have been removed entirely from price caps).[9] It is indisputable that market forces are *not* constraining the Bells' special access pricing behavior.

**The Public Interest Harms.** The record developed by the members of the Special Access Reform Coalition removes any possible doubt as to the severe public interest harms that flow from deregulating the Bells where there are not price-constraining alternatives. By allowing the Bells to charge supra-competitive special access rates, there is necessarily a reduction in investment by the wireline and wireless carriers that must rely on those special access services.[10] This, of course, leads to less innovation in services that use special access as an input. In addition, because carriers that must purchase the Bells' special access services use those services to provide at "retail" services in intensely competitive markets, a large portion of the Bells' excessive charges are ultimately passed on to the end-user customers of these carriers. It should therefore be clear that special access is not merely a "carrier-to-carrier" problem. Indeed, in many instances businesses are direct purchasers of the special access services provided by the Bells. By any measure, the Bells' special access charges also amount to a multi-billion dollar tax on U.S. businesses that imposes an enormous drag on the American economy.[11]

Moreover, the Bells increasingly have the ability to use their last mile bottleneck facilities to harm competition in downstream markets. Special access is a critical input to *all* suppliers of wireless, broadband, and long distance services. Now that the Bells have gained entry into all of these markets, the Bells have the incentive and ability to leverage their special access bottlenecks to harm competition and consumers. Allowing this to happen would be a clear abdication of the Commission's core responsibility to protect the public interest.

The potential harms go well-beyond traditional long distance markets. Special access is a critical input for next generation broadband services.[12] The deployment of more advanced services to low density business locations currently is thwarted by the excessive rates for special access services. Absent prompt Commission action, the Bells have the clear incentive and ability to price squeeze interLATA broadband rivals,[13] which, if nothing else, should trigger the Commission's stated commitment to stand "alert and ready to act against anticompetitive risks and discriminatory provisioning by dominant providers" that could threaten broadband

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[8] Commenters from a variety of market segments report that the Bells have been unwilling to negotiate and reduce price or improve quality in order to meet competition. *See, e.g.*, Ad Hoc Comments at 3; AT&T Wireless at 6; Arch Wireless at 4; Cable & Wireless Reply at 11; Pae Tec at 4; XO at 5; XO Reply at 9-10.

[9] *See, e.g.*, AT&T Petition at 12; AT&T Reply at 22-23.

[10] AT&T Reply, Ordover-Willig Reply Dec. ¶ 6.

[11] AT&T Petition at 3.

[12] *See* Cable & Wireless at 7-10.

[13] The Bells have recently announced plans aggressively to market "enterprise" services to multi-location business customers that currently buy (or potentially would buy) such services. *See* http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=77993.

competition.[14] Wireless competition too is threatened for these same reasons because independent wireless companies depend upon the Bells for high capacity transport to connect cell sites to their switches.[15] In fact, dedicated transport is the single biggest operating expense for wireless carriers. AT&T Wireless at 4.

**The Commission's Obligation to Act.** The law is clear that the Commission can no longer stand on the sidelines while the Bells continue to reap monopoly profits. Just as the Commission was entitled to rely on its "predictive judgment" that the threat of future competition would ensure that the Bells' special access rates are just and reasonable, it is now required to address the evidence that shows that the prediction was wrong. "The Commission's necessarily wide latitude to make policy based upon predictive judgments deriving from its general expertise implies a correlative *duty* to evaluate its policies over time to ascertain whether they work – that is, whether they actually produce the benefits the Commission originally predicted they would."[16] Indeed, the D.C. Circuit has specifically "emphasize[d] the need for the Commission to vigilantly monitor the consequences of its rate regulation rules" where, as here, "the Commission itself has recognized the tentative nature of its predictive judgments."[17] The Commission cannot lawfully maintain the *status quo*.

**The Required Action**. The comments already provide an overwhelming record that would support permanent rule changes establishing effective regulation of the Bells' special access services. Even before permanent new rules take effect, however, the Commission should take immediate action to provide meaningful interim relief.

The Commission should immediately establish two forms of interim relief. First, the Commission should institute a moratorium on all new pricing flexibility petitions. The evidence demonstrates that pricing flexibility is having substantial unintended consequences, in the form of higher rates and other anticompetitive terms that foreclose competition. There is overwhelming evidence that pricing flexibility has harmed the market, and that the current rules should be revisited. To ensure that these harmful effects do not spread to other MSAs, the Commission should call an immediate halt to all further pricing flexibility petitions, until the Commission can conduct a comprehensive review of the current rules.[18]

Second, the Commission should also provide immediate rate relief by bringing all special access services in existing Phase II MSAs back within price caps. The Commission has ample

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[14] *Wireline Broadband Classification NPRM* ¶ 5.

[15] *See, e.g.,* Arch Wireless at 3-4; AT&T Wireless at 2-3; *Ex Parte Letter* from Doug Bonner (T-Mobile) to Marlene Dortch, at 1 (Jan. 6, 2003) ("T-Mobile *Ex Parte*").

[16] *Bechtel* v. *FCC*, 957 F.2d 873, 881 (D.C. Cir. 1992) (emphasis added).

[17] *ACLU* v. *FCC*, 823 F.2d 1554, 1565 (D.C. Cir. 1987).

[18] *See, e.g., Western Coal Traffic League* v. *Surface Transportation Board*, 216 F.3d 1168, 1173-74 (D.C. Cir. 2000); *Neighborhood TV Co.* v. *FCC*, 742 F.2d 629, 645-50 (D.C. Cir. 1984); *Lincoln Tel. & Tel. Co.* v. *FCC*, 659 F.2d 1092, 1107-08 (D.C. Cir. 1981); *Kessler* v. *FCC*, 326 F.2d 673, 679-85 (D.C. Cir. 1963); *see also U.S.* v. *Southwestern Cable Co.*, 392 U.S. 157, 179-80 (1968) (FCC power to preserve a situation pending a determination in a broader proceeding).

authority to adopt such rate relief.[19] And the Commission should make clear that this rate relief does not trigger *any* termination liabilities or other penalty provisions of the "OPP" plans that the Bells have used to lock up customers so that alternative facilities will not be deployed even on the minority of routes where that might otherwise be economically feasible.[20]

Special access rate reform is a textbook example of the principle that justice delayed is justice denied. There is simply no other issue pending before the Commission where the stakes are higher, the public interest benefits from prompt and decisive regulatory reform will be greater, or the Commission's legal obligation to act are more clear.

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[19] The Commission has made clear that price caps do not constitute a Section 205 prescription. *See e.g., Policy and Rules Concerning Rates for Dominant Carriers,* Report and Order, 4 FCC Rcd. 2873, ¶¶ 894-95 (1989). In any event, Section 205 requires only "fair notice of, and full opportunity to comment on, the issues raised concerning the appropriate level of future rates," which has already occurred in the comments on AT&T's Petition. *See AT&T Corp. v. Business Telecom Inc.*, 16 FCC Rcd. 12312, ¶ 15 (2001).

[20] *See Local Exchange Carriers' Individual Case Basis DS3 Service Offerings*, CC Docket No. 88-136, 4 FCC Rcd. 8634, ¶ 79 (1989) (in ordering LECs to convert all individual case basis pricing for DS3 services to generally available rates, the Commission found that "we will not permit LECs to assess converted ICB customers termination liability charges or non-recurring charges").

Respectfully submitted,

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